151 FERC ¶ 61,196
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Norman C. Bay, Chairman;
Philip D. Moeller, Cheryl A. LaFleur,
Tony Clark, and Colette D. Honorable.

ISO New England Inc. Docket No. ER08-633-003

ORDER ON REMAND AND ESTABLISHING BRIEFING SCHEDULE

(Issued June 2, 2015)

1. On remand, the Commission revisits the question of whether the "Proration Rule" in ISO New England Inc.'s (ISO-NE) Transmission, Markets and Services Tariff (Tariff) allowed ISO-NE to prohibit certain suppliers needed for reliability from electing to prorate, or reduce, their quantity of megawatts offered into the Forward Capacity Auction (FCA) and to also require those suppliers to accept a prorated price. In its Initial and Rehearing Orders addressing the Proration Rule, the Commission determined that the Rule indeed allowed that result.[1] On appeal, however, the United States Court of Appeals for the District of Columbia Circuit (D.C. Circuit or court) found that the Proration Rule is ambiguous and directed the Commission to determine whether it wishes to affirm its prior interpretation "knowing that other options are permissible."[2] In this order, the Commission reverses its prior determination in its previous orders and finds that, given that ISO-NE had prohibited resources needed for reliability from prorating quantity based on its interpretation of the Proration Rule, it is appropriate to consider resettlements to those resources that were not able to prorate quantity. Accordingly, we further establish a briefing schedule to develop a better record on this question of resettlements.

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[1] *ISO New England Inc.*, 123 FERC ¶ 61,290 (2008) (Initial Order), *order denying reh'g and on informational filing*, 130 FERC ¶ 61,235 (2010) (Rehearing Order).

[2] *PSEG Energy Resources & Trade LLC AND PSEG Power Connecticut LLC v. FERC*, 665 F.3d 203, 209 (D.C. Cir. 2011) (Remand Order).

I. Background

A. FCM and Relevant Tariff Provisions

2. On March 6, 2006, ISO-NE filed a Settlement Agreement establishing the framework for New England's Forward Capacity Market (FCM).[3] Under the FCM mechanism, ISO-NE makes capacity payments to resources that provide capacity to the New England region, and capacity resources compete to be selected to provide capacity (and receive payments) on a three-year forward basis through the FCA held every year. The amount of capacity that ISO-NE must procure in each FCA is referred to as the Installed Capacity Requirement (ICR), and, as discussed below, ISO-NE's tariff prohibited ISO-NE from procuring capacity in excess of the ICR. The FCA is a descending clock auction: each capacity supplier submits an offer or de-list bid that is the lowest price that it will accept in order to provide capacity. In each round of the auction, the price is lowered, and bidders leave the auction as the price decreases below their offers or de-list bids until only enough capacity remains in the auction to meet the ICR. At that point the auction stops, and all capacity resources remaining in the auction receive the auction clearing price in exchange for their must-offer requirement in the energy market for the relevant year.

3. In addition, in the settlement establishing the FCM, ISO-NE and other settling parties agreed to use, for the first several auctions, a price floor below which the capacity clearing price could not fall.[4] Thus, at all times relevant to this order, ISO-NE's Tariff imposed two requirements: (1) ISO-NE could not purchase more capacity than the ICR; and (2) the capacity clearing price could not fall below the price floor, which was 0.6 times the Cost of New Entry (CONE),[5] which meant that when the price decreased to that floor, the FCA would terminate. These two requirements had the potential to conflict because the auction could terminate at the price floor, even though there was still excess

[3] *See generally Devon Power LLC*, 115 FERC ¶ 61,340 (FCM Settlement Order), *order on reh'g*, 117 FERC ¶ 61,133 (2006) (FCM Rehearing Order).

[4] *Devon Power, LLC*, Settlement Agreement (FCM Settlement), Section III.G.4 (Docket Nos. ER03-563-000, -030, and -055) filed March 6, 2006. The price floor ended with the eighth Forward Capacity Auction in February 2014. *ISO New England Inc.*, 142 FERC ¶ 61,107 (2013).

[5] The FCM Settlement provided that, for the first auction, CONE would be set administratively at $7.50/kW-month. FCM Settlement, section III.F. Thus, the floor price for the first auction was $4.50/kW-month.

capacity available. The Proration Rule at issue in this proceeding, implemented at Tariff section III.13.2.7.3(b), was intended to address that specific situation. It stated:

> The Capacity Clearing Price shall not fall below 0.6 times CONE. Where the Capacity Clearing Price reaches 0.6 times CONE [i.e., the floor price is reached and the auction must end], offers shall be prorated such that no more than the [ICR] is procured in the [FCA] as follows: the total payment to all listed capacity resources during the associated Capacity Commitment Period shall be equal to [the floor price] times the Installed Capacity Requirement . . . . Payments to individual listed resources shall be prorated based on the total number of MWs of capacity clearing in the Forward Capacity Auction . . . . Suppliers may instead prorate their bid MWs of participation in the Forward Capacity Market by partially de-listing one or more resources . . . . Any proration shall be subject to reliability review.

B. Initial Order

4. As discussed in the Initial Order, ISO-NE conducted its first FCA on February 4-6, 2008 (FCA 1), and, on March 3, 2008, ISO-NE submitted those auction results to the Commission.[6] In that filing, ISO-NE stated that it had procured capacity equal to the region's Net ICR[7] of 32,305 MW and that, because the auction cleared at the floor price of $4.50/kW-month with excess capacity above the Net ICR, "proration of either the price of capacity or the MW provided will take place."[8] Citing to the Proration Rule, ISO-NE stated that resources either will receive a Capacity Supply Obligation[9] of their full cleared capacity at a price of $4.254/kW-month, or may elect to prorate their offers clearing in the FCA by choosing to restore the price to $4.50/kW-month and reducing their Capacity Supply Obligation by an equivalent percentage. ISO-NE

[6] Docket No. ER08-633-000 (March 3, 2008 Filing).

[7] The Net ICR is the net amount of capacity to be purchased in the FCA to meet the ICR after deducting the Hydro Quebec Interconnection Capability Credits.

[8] March 3, 2008 Filing at 2.

[9] Resources that receive a Capacity Supply Obligation through the FCA are required to offer their capacity into the Day-Ahead and Real-Time Energy Markets every day that the resource is physically available. In return for that obligation, those resources receive capacity payments.

clarified, however, that "[a]ny election to prorate a Capacity Supply Obligation is subject to a reliability review."[10] Accordingly, ISO-NE added that, "due to the relatively small transmission security margin in the Connecticut sub-area, *it is highly unlikely that the ISO will allow proration based on bid MW for resources within the Connecticut sub-area*."[11]

5. The PSEG Power Companies (PSEG), an owner of generation resources in New England and a supplier that submitted an offer into the FCA, protested the filing, arguing that "[t]he structure of the tariff makes clear that resources not allowed to prorate [due to reliability review] should be paid the otherwise applicable [unprorated] clearing price."[12] Under PSEG's view, when the auction ends because it has reached the price floor but there remains more capacity in the auction than the ICR, the Proration Rule gave each supplier the choice to either: (1) take a prorated (i.e., reduced) price for all the megawatts committed by the supplier, or (2) prorate quantity (MW), rather than price. But, PSEG asserted, the choice only applies when the Proration Rule is triggered from the outset.[13] PSEG maintained that, while the Tariff provided for proration in the absence of reliability concerns, the last sentence of the Proration Rule providing for reliability review governed the earlier sentence providing that resources "shall" be prorated. Thus, according to PSEG, "because the proration price/volume reduction provision is expressly 'subject to' the reliability review, the entire proration mechanism does not apply [from the outset] if the units are needed for local reliability reasons,"[14] and instead "the 'reliability review' provision . . . *prevents* the proration mechanism (including the price modification provision) from becoming operable,"[15] so that there would be, in fact, no proration. PSEG asserted that in that circumstance, "the general pricing provisions, i.e., the general Market Clearing Price mechanism, must be controlling," so that ISO-NE must pay all

[10] *Id.* at 8.

[11] March 3, 2008 Filing at 11-12, emphasis added, footnote omitted. ISO-NE subsequently confirmed that determination in a filing made on November 18, 2008, which the Commission accepted. Rehearing Order, 130 FERC ¶ 61,235 at P 45.

[12] PSEG Protest at 8.

[13] *Id.*

[14] *Id.*

[15] *Id.*, emphasis in original.

resources that are needed for reliability the full market clearing price for each megawatt of their capacity commitment.[16]

6. In the Initial Order, the Commission accepted the results of FCA 1, rejecting PSEG's interpretation of the Proration Rule and of the final sentence, "[a]ny proration shall be subject to reliability review." The Commission found that PSEG's interpretation would violate the tariff and the FCM Settlement,[17] both of which limited the total payment for capacity to the amount equal to the ICR multiplied by the clearing price. The Commission explained that the FCM Settlement thus imposed a cap on the total payment that customers would be required to make for capacity, and PSEG's interpretation would violate that cap. The Commission stated that, to ensure the total payment cap is not exceeded, ". . . ISO-NE is required by the FCM Settlement and the FCM rules to prorate either the price or capacity obligation of resources that cleared in the auction."[18] The Commission further held that: "[i]f, as is likely with Connecticut resources, allowing resources to prorate their MWs would violate reliability criteria . . . , the FCM rules are clear that such resources will only be allowed to prorate the price they receive and not their MW capacity obligation."[19]

C. Request for Rehearing and Rehearing Order

7. PSEG sought rehearing of the Initial Order, largely reiterating its previous arguments that, once the Connecticut resources were found to be needed for reliability, they should be paid the full market clearing price under the language of the Proration Rule. PSEG argued that the Commission had misinterpreted the Proration Rule, and that under the correct interpretation, if resources were prevented from prorating quantity for reliability reasons, those resources should not be required to accept price proration.[20] It argued that it would be illogical to interpret the Tariff as applying some form of proration (either quantity or price proration) to all resources, with reliability review relevant to determining only which choice of proration method applies to a particular resource. PSEG posited that only quantity proration – providing fewer megawatts – could impact reliability, while paying resources a lower price would not. Thus, according to PSEG, the

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[16] *Id*.

[17] FCM Settlement, section III.G.4.

[18] Initial Order, 123 FERC ¶ 61,290 at P 74.

[19] *Id*. P 75.

[20] PSEG Rehearing Request at 5.

provision that "[a]ny proration shall be subject to reliability review" must be read as an exemption of sorts, so that resources needed for reliability would not be subject to any proration at all.

8. Moreover, PSEG argued, the Commission's interpretation of the Proration Rule results in undue discrimination against resources needed for reliability by prohibiting only them from choosing quantity proration which causes them to be paid less than other resources. PSEG further posited that forcing price proration upon resources needed for reliability – which are necessarily located in regions where their capacity makes the largest contribution to system reliability – frustrated the primary policy goal of FCM, which PSEG viewed as providing incentives for existing resources to remain in constrained areas and for new resources to locate there.

9. The Commission denied PSEG's request for rehearing. It stated that when a reliability violation would occur due to quantity proration, the Proration Rule "does not allow ISO-NE to meet the requirement that total payment to listed resources equals ICR multiplied by 0.6 times CONE without price proration, and [PSEG's] interpretation would violate the requirements of section III.13.2.7.3 of the Tariff."[21]

10. The Commission also rejected PSEG's view that when ISO-NE prorates capacity offers during an auction, this is the effective equivalent of a de-listing request, thus entitling a supplier under the Tariff to out-of-market compensation. The Commission stated that:

> Under the current market rules, de-listing and proration occur at different points during the overall process of obtaining capacity, and are governed by different tariff provisions, including the provisions governing compensation for bids that cannot de-list and bids that are required to prorate. It would thus violate the tariff to compensate proration as if it were governed by the de-listing tariff provisions.[22]

[21] Rehearing Order, 130 FERC ¶ 61,235 at P 41. The Commission further noted that, when the sentence "any proration shall be subject to reliability review" was added to section III.13.2.7.3(b), no party protested the addition of that language. *Id*., P 41 n.40.

[22] *Id*., P 41.

D. Remand Order

11. PSEG appealed the Commission's Initial and Rehearing Orders to the U.S. Court of Appeals for the D.C. Circuit, and the court remanded the case to the Commission.[23] Applying a two-step "*Chevron*-like analysis,"[24] the court first turned to the question of whether the final sentence of the Proration Rule ("Any proration shall be subject to reliability review.") "compels" the meaning that the Commission attributed to it. The court noted that in rejecting PSEG's interpretation of that sentence, the Commission "spoke the language of textual clarity" in finding that "the [FCM] rules are clear" and "the current tariff language does not allow" PSEG's interpretation.[25] The court found, however, that the "rule's final sentence does not explain how [ISO-NE] will conduct its review or what [ISO-NE's] next step will be if it determines that reliability is in peril."[26] The court stated that "the rule does not unambiguously proclaim FERC's position that the total payment cap [*i.e.*, the number of MW in the ICR, times the floor price] is sacrosanct even during reliability review,"[27] rather than PSEG's position that the phrase "any proration shall be subject to reliability review" means that resources that are required to maintain reliability should not be subject to any proration at all, whether of price or quantity.

12. Finding that the last sentence of the Proration Rule was ambiguous, the court remanded the case to permit the Commission to exercise its discretion as to "whether it wishes to retain its interpretation knowing that other options are permissible," including

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[23] Remand Order, 665 F.3d 203 at 209.

[24] *Id.* at 208 (referring to *Chevron U.S.A. Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837 (1984) (*Chevron*) and citing *Colorado Interstate Gas Co. v. FERC*, 599 F.3d 698, 701 (D.C. Cir. 2010) (*Colorado Interstate Gas*) (the court must first "consider *de novo* whether the [tariff] unambiguously addresses the matter at issue. If so, the language . . . controls for we must give effect to the unambiguously expressed intent of the parties. . . . If the tariff language is ambiguous, we defer to the Commission's construction of the provision at issue so long as that construction is reasonable").

[25] Remand Order, 665 F.3d 203 at 208, citing Initial Order, 123 FERC ¶ 61,290 at P 75 and Rehearing Order, 130 FERC ¶ 61,235 at P 41.

[26] *Id.*, 665 F.3d 203 at 209 (citation omitted).

[27] *Id.*

whether PSEG's interpretation is "appropriate."[28] The court further noted that, following issuance of the Initial and Rehearing Orders, ISO-NE had revised its Tariff with language reflective of PSEG's position here, and the Commission accepted those changes "as an improvement."[29]

13. The court further found that the Commission had failed to respond to PSEG's arguments that (a) ISO-NE's interpretation would result in "undue discrimination" because resources most needed for reliability would be paid less per unit than other resources, and (b) ISO-NE's interpretation was inconsistent with what PSEG described as the policy goals of the FCM, namely, to provide incentives for resources to remain in or enter constrained areas.[30] The court directed the Commission to respond to those arguments, stating that the "objections on their face seem legitimate."[31]

II. Discussion

14. We have revisited our analysis of the Proration Rule in light of the court's opinion, particularly its view that the Proration Rule is ambiguous, and on remand, we reverse our earlier determination. We now find that where resources needed for reliability were prohibited from prorating quantity under the Proration Rule, they should have received the full market clearing price for each megawatt offered. However, for the reasons discussed below, we agree that ISO-NE's interpretation that the Proration Rule barred resources needed for reliability from prorating capacity was appropriate.

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[28] *Id*., 665 F.3d 203 at 209-10 (citations omitted). The court explained that it could not proceed to analyze whether the Commission had reasonably exercised its discretion in interpreting the final sentence of the Proration Rule, because, having erroneously found that the final sentence clearly required the outcome in its Initial Order, the Commission had not exercised discretion at all.

[29] *ISO New England Inc.*, 131 FERC ¶ 61,065, at P 163 (2010). Under the new language, all proration is subject to reliability review by ISO-NE, and if the option to prorate a particular resource's megawatts is rejected for reliability reasons, that resource will be paid the full capacity clearing price for each of the megawatts that clear in the auction. The difference between the resource's actual payment, and what the payment would have been had proration of the resource not been rejected for reliability reasons, is allocated to load within the affected reliability region.

[30] Remand Order, 665 F.3d 203 at 209-210.

[31] *Id*., 665 F.3d 203 at 210.

15. The Proration Rule states that "[s]uppliers may instead [of prorating price] prorate their bid MWs of participation in the Forward Capacity Market by partially de-listing one or more resources." While the use of the word "may" in that sentence can communicate that prorating quantity is a possible alternative to the default mechanism (price proration), the choice is not unqualified. Rather, the next and final sentence states that "[a]ny proration shall be subject to reliability review."[32] We find that ISO-NE reasonably interpreted that sentence within the context of the Proration Rule as allowing it to limit certain suppliers' ability to prorate quantity, in order to maintain reliability.

16. While we continue to disagree with PSEG's argument that it would be unduly discriminatory under the Federal Power Act (FPA)[33] to make unavailable to certain resources (such as, resources needed for reliability) the option to choose quantity proration instead of price proration (as it is well-established that the FPA prohibits only *undue* discrimination[34]), as discussed below, our rejection of PSEG's arguments on this issue does not adversely affect PSEG's ultimate interest in this case, as we further find that resources prevented from prorating quantity must also receive a just, reasonable, and not unduly discriminatory or preferential rate, and, specifically the full clearing price for each megawatt offered.

17. Thus, we turn to the next question: having determined that the ambiguous language of the Proration Rule allowed ISO-NE to prohibit resources needed for reliability from prorating quantity, must those resources then accept a prorated price? As the court notes, the Proration Rule did not clearly state what action ISO-NE would take subsequent to the reliability review provided for in the last sentence. Contrary to the determination in the Initial Order, we here find that ISO-NE could not properly force

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[32] ISO-NE added that final sentence to the Proration Rule in a filing made on August 31, 2007. That filing was not protested, and the Commission accepted it without any discussion on October 30, 2007. *ISO New England Inc.*, 121 FERC ¶ 61,106 (2007).

[33] 16 U.S.C. § 824d (2012).

[34] *St. Michaels Utils. Comm'n v. FPC*, 377 F.2d 912, 915 (4th Cir.1967) ("differences in rates are justified where they are predicated upon differences in facts – costs of service or otherwise – and where there exists a difference in rates which is attacked as illegally discriminatory, judicial inquiry devolves on the question of whether the record exhibits factual differences to justify classifications among customers and differences among the rates charged them"); *Otter Tail Power Co.*, 2 FPC 134, 141, 145 (1940). *Cf. United States v. Chicago Heights Trucking Co*., 310 U.S. 344, 351, 60 S.Ct. 931, 935, 84 L.Ed. 1243, 1247-1248 (1940).

such resources to accept a prorated price, as doing so would result in rates that are unjust and unreasonable.

18. The Commission is statutorily mandated to ensure that rates for service within its jurisdiction are just and reasonable, and it cannot approve a tariff that "grants undue preference or advantage to any person or subject[s] any person to any undue prejudice or disadvantage, or . . . maintain[s] any unreasonable difference in rates . . . as between classes of service.[35] Considering its statutory mandate in conjunction with the principle that ambiguous tariff language should, if possible, be interpreted in such a fashion as to render it lawful rather than unlawful,[36] the Commission does not read the Proration Rule, in particular the last sentence therein, as requiring that, where resources are needed for reliability and cannot prorate quantity, they must also accept a prorated price. We find that such an interpretation would result in unjust, unreasonable, and unduly discriminatory rates for resources located in constrained areas.

19. Under this interpretation, the Connecticut resources that were prevented from prorating quantity, but were paid a prorated price, will receive treatment that is different from that accorded other resources. However, as noted above, the FPA prohibits only "undue" discrimination, not all discrimination. As the D.C. Circuit recently stated, "[w]e accept disparate treatment between ratepayers only if FERC 'offer[s] a valid reason for the disparity,'"[37] and the Commission may "identif[y] valid reasons by pointing to differences between parties that are relevant to the achievement of permissible policy goals."[38] Here, the Connecticut resources were not similarly situated to other resources, in two ways: (1) because they were located in constrained areas, ISO-NE could prevent

[35] 16 U.S.C. § 824d(b) (2012).

[36] *See Papago Tribal Utility Authority v. FERC*, 723 F.2d 950, 954 (D.C. Cir. 1983).

[37] *Black Oak Energy, LLC v. FERC*, 725 F.3d 230, 239 (D.C. Cir. 2013) (citing *Electricity Consumers Resource Council v. FERC*, 747 F.2d 1511, 1515 (D.C.Cir.1984) (internal quotation marks omitted)).

[38] *Black Oak Energy*, *supra*, 725 F.3d at 239 (citing *Transmission Agency of N. Cal. v. FERC*, 628 F.3d 538, 549 (D.C.Cir.2010) ("The court will not find a Commission determination to be unduly discriminatory if the entity claiming discrimination is not similarly situated to others" (citation omitted))). *See also Ark. Elec. Energy Consumers v. FERC*, 290 F.3d 362, 367 (D.C.Cir.2002) ("A rate is not unduly preferential or unreasonably discriminatory if the utility can justify the disparate effect" (internal quotation marks omitted)).

them from reducing quantity without effecting undue discrimination against them; however, (2) because they were needed for reliability and could not reduce quantity under the Proration Rule, they should receive the non-prorated market clearing price, which would not be an undue preference when compared to other resources.

20. We next turn to PSEG's additional policy argument that paying resources needed for reliability less per unit than other resources is inconsistent with what PSEG described as the goals of the FCM, namely, to incent new entry and retain resources in constrained areas. Because we here find that under the FPA, the relevant resources should be paid the full, non-prorated price, PSEG's policy argument is moot.

21. As discussed above, the FCM Settlement and ISO-NE's tariff provisions placed a limit on the amount that customers would be required to pay for capacity (i.e., load would not have to purchase, and pay for, more capacity than what is equal to the ICR times the clearing price). However, after the Commission accepted both the FCM Settlement and ISO-NE's tariff provisions implementing it, ISO-NE later added the Proration Rule, to ensure that reliability targets are met. The Commission now rules that, so as to ensure that our interpretation of this tariff provision is consistent with the FPA's prohibition on undue discrimination, it is appropriate to look at possible resettlements for PSEG and other Connecticut generators that were not able to prorate quantity. We will establish a briefing schedule to permit the parties to address issues relating to the amounts of such resettlements (i.e., the difference between a resource's actual payment and what the payment would have been had proration of the resource not been rejected for reliability reasons), and the parties to which those payments should be charged and to whom they should be paid (taking into consideration any possible changes in ownership, retirements, or similar new circumstances of the resources in question). Further briefing on these issues will help develop a more complete record to better determine appropriate resettlements.

22. We will require ISO-NE, and any other interested parties, to submit initial briefs on or before 45 days from the issuance date of this order, and ISO-NE or any other party that wishes to reply may submit a reply brief on or before 30 days following the due date of the initial briefs.

23. In the initial briefs, we will require ISO-NE to address, and permit other parties to address, the following questions:

a) the identities of the Connecticut resources that were unable to prorate quantity in the first FCA, and the number of megawatts for which each resource received a capacity obligation;

b) any resettlements due to each such entity, based on the difference between (1) the prorated price that the resources did receive, and (2) the un-prorated capacity clearing price that the resources would have received absent price proration, plus interest;

c) the parties to whom the resettlements should be charged. In particular, we will require ISO-NE to address whether those resettlements should be charged to Regional Network Load within the affected Reliability Region, consistent with the current version of the Proration Rule, ISO-NE's current tariff section III.13.2.7.3(b)(iv), which provides that (emphasis added) "[w]here proration is rejected for reliability reasons, the resource's payment shall not be prorated as described in subsection (ii) above, and the difference between its actual payment based on the Capacity Clearing Price and what its payment would have been had prorationing not been rejected for reliability reasons *shall be allocated to Regional Network Load within the affected Reliability Region*";

d) the mechanism by which ISO-NE intends to make such resettlements; and

e) any considerations that would render the resettlements inappropriate or difficult.

24. Parties other than ISO-NE are free to, but not required to, address the above issues.

The Commission orders:

(A) The Initial Order and Rehearing Order are hereby reversed, as discussed in the body of this order.

(B) ISO-NE is hereby directed to submit, and interested parties may file, an initial brief within 45 days of the date of this order, as discussed in the body of this order. ISO-NE and interested parties may file reply briefs within 30 days of the date initial briefs are due, as discussed in the body of this order.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.